No. 14,972

United States Court of Appeals

For the Ninth Circuit

James F. Crafts,

Appellant,

vs.

Federal Trade Commission,

Appellee.

APPELLANT'S OPENING BRIEF.

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JURISDICTION.

This is an appeal from an order enforcing a *subpena duces tecum* issued by the Federal Trade Commission in an adjudicative or quasi-judicial proceeding against Fireman's Fund Indemnity Company. The subpena was directed to appellant, James F. Crafts, who is President of the Company.

Jurisdiction of the District Court is set forth in Section 9 of the Federal Trade Commission Act, 38 Stat. 722, 15 U. S. C. 49, and in Section 6(c) of the Administrative Procedure Act, 60 Stat. 240, 5 U. S. C. 1005(c).

The order enforcing the subpena is a final decision of the District Court and the appellate jurisdiction is set forth in the Judicial Code, 62 Stat. 929, 28 U. S. C. 1291.

STATEMENT OF THE CASE.

The purpose of this proceeding is to secure a judicial interpretation of Public Law 15, 79th Congress (59 Stat. 31, 15 U. S. C. 1011-1015) and thereby determine what authority or jurisdiction, if any, the Federal Trade Commission has over advertising of accident and health insurance policies. Tr. 38. The pertinent portion of Public Law 15 provides that the Federal Trade Commission may regulate the business of insurance only "to the extent that such business is not regulated by State law". Tr. 35.

This case results from an adjudicative or quasi-judicial proceeding in which the Federal Trade Commission seeks to regulate advertising of accident and health insurance policies by Fireman's Fund Indemnity Company. Tr. 8-20. The Company denies that any advertising issued by it was or could be misleading or deceptive. Tr. 56, 59 and 60. The Company further denies that the Federal Trade Commission has any authority or jurisdiction to regulate any of the Company's advertising and claims that all of its advertising is regulated by State law. Tr. 24 and 34-38. The Company is a California corporation licensed by and doing business in each of the forty-eight States and the District of Columbia. Tr. 8, 36-37 and 53. The Company contends that its advertising is regulated not only by the State law of California but also by the local laws of the other forty-seven States and of the District of Columbia. Tr. 36-37.

This appeal does not involve the merits of the administrative proceeding. But this court, in order to determine if the evidence sought by the subpena is competent or relevant to any lawful purpose of the Commission (*Pen-*

field Co. of California v. Securities and Exchange Commission, 9 Cir., 143 F. 2d 746, 751, cert. den. 323 U. S. 768), must consider the extent (if any) that advertising by Fireman's Fund "is not regulated by State law". As Senator McCarran, author of Public Law 15, said (94 Congressional Record No. 11, p. A 3214) the inquiry should be "Is this practice regulated by state law? Not, is it effectively regulated or is it wisely regulated; but simply is it regulated?". Tr. 35. If the practice, to wit, advertising of accident and health insurance policies by Fireman's Fund is regulated by State law everywhere, then, in our opinion, the Federal Trade Commission as a matter of law does not have any authority or jurisdiction to regulate such advertising anywhere and the evidence cannot be competent or relevant "to any lawful purpose of the Commission" as required by the *Penfield* case.

The Federal Trade Commission does not claim any power to regulate advertising by Fireman's Fund in California but does claim jurisdiction to regulate such advertising in all other states and in the District of Columbia. Tr. 36, 39 and 42. This claim is made despite the local laws, most of which are "model acts" designed for the very purpose of preserving state regulation as opposed to Federal Trade Commission regulation. Tr. 42. This claim of jurisdiction over Fireman's Fund in all states except California is based, as we understand it, on the theory that the Federal Trade Commission can regulate advertising in any state other than the domiciliary state even though the other state has full regulation. Tr. 89. We believe this is contrary both to the letter and to the spirit of Public Law 15.

It must be remembered that Public Law 15 was passed almost immediately after the Supreme Court in *U. S. v. South-Eastern Underwriters,* 322 U. S. 533 (1944), held that insurance was commerce, contrary to the 1868 decision in *Paul v. Virginia,* 8 Wall. 168. Tr. 34-35 and 65-66. The Company believes that Congress in passing Public Law 15 intended to restore to the states full power to regulate the business of insurance and to divest the Federal Trade Commission of power which otherwise might come from the *South-Eastern Underwriters* decision. Therefore, the Company has claimed from the beginning (Tr. 37) and still claims (Tr. 24-25) that the Federal Trade Commission has no jurisdiction in the pending proceeding because of regulation by state law. When the subpena was served on Mr. Crafts the Company moved to quash or in the alternative to limit it to evidence regarding activities in those states (if any) which had no regulatory statute. Tr. 27. The Hearing Examiner denied the motion to quash and denied the alternative motion to limit except as to California. The Company appealed to the Commission which affirmed the Hearing Examiner. Tr. 27.

The subpena was for a hearing in San Francisco on October 17, 1955. Tr. 20. Mr. Crafts was the first witness called on behalf of the Commission. Tr. 33. He identified himself as the President of the Company and then refused to give further testimony or to produce any documents on the ground that the Federal Trade Commission had no jurisdiction over Fireman's Fund because of regulation by State law, but offered to do so if and when the proper courts finally determine that the Commission has jurisdic-

tion over the advertising of accident and health insurance policies issued by the Company. Tr. 33-38. Counsel for the Company pointed out that the only method known to him of securing a determination of this question at that stage of the proceeding would be in an action by the Federal Trade Commission requesting the District Court to enforce the subpena. Tr. 38. The administrative proceeding was then continued to permit the Commission to file such an action. Tr. 44-45. It was stipulated prior to the continuation that the outcome of this action would apply equally to other Company officials. Tr. 43-44.

The action was filed the next day, October 18, 1955, in the District Court of the United States for the Northern District of California, Southern Division. Tr. 3-7. The answer alleging no jurisdiction was filed on October 20 (Tr. 24-25) and the case was immediately placed on the trial calendar by stipulation. It was assigned to the Honorable Oliver D. Hamlin for trial, but was continued by him until October 21 because he was concluding another matter.

At the outset of the trial on October 21 (Tr. 51, 62-63) this case became not only a test of Public Law 15 but also a test of Section 6(c) of the Administrative Procedure Act (60 Stat. 240, 5 U. S. C. 1005(c)), which provides that upon contest the court shall sustain any such subpena "to the extent that it is found to be in accordance with law". The District Court interpreted this to mean that a subpena must be enforced merely because it was issued with due formality and refused to consider what jurisdiction (if any) the Federal Trade Commission had over advertising by Fireman's Fund of accident and

health insurance policies and refused to consider if the evidence sought by the subpena was or could be material or relevant to any lawful proceeding by the Commission. Tr. 70, 77, 82-83. The Court thereupon issued the order enforcing the subpena but the order was stayed without objection pending final determination on appeal. Tr. 96-97.

SPECIFICATION OF ERROR.

We believe the action of the District Court in interpreting Section 6(c) as precluding any consideration into the lawfulness of the administrative proceeding or into the jurisdiction (if any) of the Commission to regulate a particular activity is contrary to law and might violate the Fourth Amendment. Our belief finds support in the legislative history of the Administrative Procedure Act and in the judicial decisions which have considered administrative subpenas.

Therefore, as we said before, this appeal is a test not only of Public Law 15, but also of Section 6(c) of the Administrative Procedure Act.

ARGUMENT.

A DISTRICT COURT SHOULD CONSIDER IF THE ADMINISTRATIVE PROCEEDING IS LAWFUL BEFORE ENFORCING A SUBPENA ISSUED IN SUCH PROCEEDING.

Section 6(c) of Administrative Procedure Act provides:

> "(c) Agency subpenas authorized by law shall be issued to any party upon request and, as may be required by rules of procedure, upon a statement or

showing of general relevance and reasonable scope of the evidence sought. Upon contest the court shall sustain any such subpena or similar process or demand to the extent that it is found to be in accordance with law and, in any proceeding for enforcement, shall issue an order requiring the appearance of the witness or the production of the evidence or data within a reasonable time under penalty of punishment for contempt in case of contumacious failure to comply." 60 Stat. 240, 5 U. S. C. 1005(c).

The District Court interpreted the phrase "in accordance with law" as precluding any consideration of the lawfulness of the administrative proceeding; in other words, as precluding consideration of the defense that the Federal Trade Commission has no jurisdiction as a matter of law. The District Court held that the subpena must be enforced merely because it was issued and served with due formality. This, in our opinion, is contrary to law.

The phrase "in accordance with law" is not defined in the Administrative Procedure Act. However, its meaning seems clear when we consider the law as it stood when the Act was passed and also consider the legislative history as set forth in Senate Document No. 248, 79th Congress, 2d Session. Beginning with the Interstate Commerce Commission in 1887, 49 U. S. C. 1, et seq., it has been a conventional feature of congressional regulatory legislation to give administrative agencies authority to issue subpenas for relevant information. However, Congress has never attempted to confer upon an administrative agency the power to compel obedience to such a subpena; instead, Congress has consistently required the

administrative agencies to resort to the courts for enforcement. The judicial function thus vested in the courts is not limited, in our opinion, merely to a determination that the subpena was signed by the proper officer or otherwise issued and served with due formality.

The Supreme Court Decisions.

The Supreme Court has been consistent in holding that "an appropriate defence" may be made to an action to enforce a subpena. *Myers v. Bethlehem Shipbuilding Corporation,* 303 U. S. 41, 49 (1938). The fact that the agency is acting beyond its authority as a matter of law would seem to be one of the most appropriate defenses to such an action.

In *Jones v. Securities and Exchange Commission,* 298 U. S. 1 (1935), the Supreme Court reversed a District Court order enforcing a subpena for the reason that the Commission lacked jurisdiction over the matters involved. The jurisdictional question hinged solely on a point of law, the issue being whether a registration statement filed by Mr. Jones might be withdrawn without first obtaining the Commission's consent. The Court held that the registration statement could be withdrawn and that by its withdrawal the Commission had lost jurisdiction.

The Court on page 25 stated its position very concisely:

> "The proceeding for a stop order having thus disappeared, manifestly it cannot serve as the basis for the order of the district court compelling petitioner to appear, give testimony, and produce his private books and papers for inspection by the commission. But the commission contends that the order may rest upon the general power to conduct investigations which it says is conferred by §19(b). The difficulty

with that is that the investigation was undertaken for the declared and sole purpose of determining whether a stop order should issue."

and on page 26 the Court said:

"The citizen, when interrogated about his private affairs, has a right before answering to know why the inquiry is made; and if the purpose disclosed is not a legitimate one, he may not be compelled to answer."

Endicott-Johnson Corp. v. Perkins, 317 U. S. 501 (1943), was mentioned by the Court below as precluding judicial consideration of jurisdiction. Tr. 68 and 77. This case did enforce an administrative subpena in a proceeding where "coverage" under the statute depended upon evidence as to whether certain employees worked on government contracts or private contracts. This was the very evidence sought by the subpena. The Court said that in such a case the District Court was not authorized to decide the question of "coverage" itself. However, the Supreme Court recognized a distinction, where, as a matter of law, the agency might be acting unlawfully or beyond its jurisdiction and said at page 509:

"The evidence sought by the subpoena was not plainly incompetent or irrelevant to any lawful purpose of the secretary in the discharge of her duties under the Act, and it was the duty of the District Court to order its production for the secretary's consideration."

In the *Endicott-Johnson* case as Mr. Justice Murphy points out in his dissent at page 512:

"The Government concedes that the District Courts are more than mere rubber stamps of agencies in

> enforcing administrative subpoenas and lists as examples of appropriate defenses * * * or that it is plain on the pleadings that the evidence sought is not germane to any lawful subject of inquiry."

Oklahoma Press Publishing Co. v. Walling, 327 U. S. 185 (1946), is sometimes cited as precluding a District Court from considering "coverage" on an application to support a subpena. Like the *Endicott-Johnson* case it involved a situation where coverage depended upon the evidence sought by the subpena. It did not involve lack of authority as a matter of law. The Supreme Court again recognized the distinction. It pointed out at p. 208 that the inquiry must be one "the demanding agency is authorized by law to make". The Court pointed out further at p. 216 that Mr. Walling, the administrator, must not act "in excess of his statutory authority".

The *Oklahoma Press* case was decided in February 1946. The Administrative Procedure Act was approved on June 11, 1946. It is fair to assume that Congress, in using the phrase "in accordance with law", did not intend to broaden agency authority or to place additional limitations upon district courts called upon to enforce administrative subpenas. In fact, the legislative history which we shall discuss later is clearly to the contrary and can be construed as directing the courts specifically to give even greater consideration to the jurisdiction of an agency before enforcing a subpena. The later Supreme Court cases do not indicate any relaxation of prior requirements.

Penfield Co. v. Securities and Exchange Commission, 330 U.S. 585 (1947), is the aftermath of a subpena. It involved contempt for failure to obey the order enforcing

the subpena. The question before the Supreme Court was whether the contempt was civil or criminal. The Court held that the contempt was civil and in doing so said, pages 591-592:

> "As we have already noted, the Act requires the production of documents demanded pursuant to lawful orders of the Commission and lends judicial aid to obtain them. There is no basis in the record before us for saying that the demand of the Commission exceeded lawful limits."

The dissenting opinion by Mr. Justice Frankfurter with whom Mr. Justice Jackson concurred was more explicit on this point. It says at pages 603-604:

> "Beginning with the Interstate Commerce Act in 1887, it became a conventional feature of Congressional regulatory legislation to give administrative agencies authority to issue subpoenas for relevant information. Congress has never attempted, however, to confer upon an administrative agency itself the power to compel obedience to such a subpoena. It is beside the point to consider whether Congress was deterred by constitutional difficulties. That Congress should so consistently have withheld powers of testimonial compulsion from administrative agencies discloses a policy that speaks with impressive significance.
>
> "Instead of authorizing agencies to enforce their subpoenas, Congress has required them to resort to the courts for enforcement. In the discharge of that duty courts act as courts and not as administrative adjuncts. The power of Congress to impose on courts the duty of enforcing obedience to an administrative subpoena was sustained precisely because courts were not to be automata carrying out the wishes of the

> administrative. They were discharging judicial power with all the implications of the judicial function in our constitutional scheme (citing authority). Accordingly, an order directing obedience to a subpoena by the Securities and Exchange Commission like a subpoena of any other federal agency, does not issue as a matter of course. An administrative subpoena may be contested on the ground . . . that the inquiry is outside the scope of the authority delegated to the agency; . . .''

Shapiro v. United States, 335 U.S. 1 (1948), involved a conviction in a criminal case after a claim of immunity based upon the production of evidence pursuant to an administrative subpena. The Court in sustaining the conviction said at page 30:

> ''It is clear that if the Administrator sought to obtain data irrelevant to the effective administration of the statute and if his right of access was challenged on the ground that the evidence sought was 'plainly incompetent or irrelevant to any lawful purpose of the Administrator', that objection could sustain a refusal by the district court to issue a subpoena or other writ to compel inspection.''

The latest case on this subject was decided less than two months ago. It is *U.S. v. Minker,* ..... U.S. ....., 100 L. ed. (Advance p. 191), and involved conflicting decisions in the second and third circuits in actions to enforce subpenas issued under Section 235(a) of the Immigration and Nationality Act of 1952, 66 Stat. 163, 198. The question presented was purely a matter of law. The section authorizes subpenas requiring the attendance and testimony of witnesses before immigration officers and special

inquiry officers and the production of books, papers and documents relating to the privilege of any person to enter, re-enter, reside in or pass through the United States, or concerning any matter which is material and relevant to the enforcement of the Act. The section further provides for enforcement by any United States District Court. Each of the subpenas in question was for the purpose of securing evidence from a citizen who was himself the subject of an investigation directed toward his denaturalization. The Supreme Court (without finding it necessary to refer to Section 6(c) of the Administrative Procedure Act) held that Congress had not granted authority to subpena the citizen who is himself the subject of the denaturalization investigation and, therefore, quashed the subpenas. The Supreme Court considered the question purely as a matter of statutory interpretation.

The same situation is presented by the present case. Fireman's Fund contends that as a matter of statutory interpretation its advertising of accident and health insurance is regulated by state law in all forty-eight states and the District of Columbia, and therefore the Federal Trade Commission has no jurisdiction to regulate such advertising anywhere. The Supreme Court in *U.S. v. Minker* reversed the court of appeals for the second circuit (219 F.2d 137) which had reversed the district court where the case was known as *Application of Barnes,* 116 F.Supp. 464 (N.D. N.Y., 1953). The district court decision, thus affirmed by the Supreme Court, specifically pointed out that a subpena should be quashed if the agency is acting beyond the authority granted by Congress. The district court said at page 467:

> "* * * The importance to the administration and enforcement of the Act is evident because it would ease the burden of investigations in such situations as here, but such reason of expediency cannot prevail if the subpena power exercised is in excess of the statutory grant. The authority of Congress to delegate the subpena power to administrative agencies is clearly established, even to the extent that it may delegate effective power to investigate violations of its own laws. However, the subpena power must remain within the bounds of the legislative grant, not overreach the authority granted by Congress, and in investigatory matters should be conferred in express and explicit terms for that purpose. Harriman v. Interstate Commerce Comm., 211 U.S. 407, 29 S.Ct. 115, 53 L.Ed. 253; Oklahoma Press Publishing Co. v. Walling, 327 U.S. 186, 201, 217, 66 S.Ct. 494, 90 L.Ed. 614; National Labor Relations Board v. Anchor Rome Mills, Inc., 5 Cir., 197 F.2d 447, 449. In my own judgment, subpenas should not issue upon hit or miss legal grounds."

In each of these cases the Supreme Court considered whether the administrative inquiry was lawful or unlawful and in two of these cases, *Jones v. Securities and Exchange Commission and U.S. v. Minker,* quashed the subpenas because the agency was acting beyond its authority or jurisdiction. These decisions (both before and after the passage of the Administrative Procedure Act) compel the conclusion that upon contest of an application to enforce an administrative subpena the District Court should hear and determine a defense based on the claim that the agency has no jurisdiction as a matter of law. This the lower court refused to do in the present case.

The refusal of the lower court to hear and determine the claim that the Federal Trade Commission has no jurisdiction as a matter of law over advertising of accident and health insurance by Fireman's Fund seems to be based primarily on *Tobin v. Banks & Rambaugh,* 5th Cir. 201 F.2d 223, Cert. den., 345 U.S. 943 (1953). The *Tobin* case like the *Endicott Johnson* case enforced an administrative subpena where the question of "coverage" depended upon the very evidence sought by the subpena. To this extent it may be correct and this may be the reason why certiorari was denied. But if the *Tobin* case decided (as some people think it did at page 225) that the phrase "in accordance with law" prohibits the District Court from considering whether the person and subject matter to which the subpena is directed are within the jurisdiction of the agency, it seems to be wrong. At least it is contrary to the decisions of the Supreme Court cited above and is contrary to the legislative history of the Act.

Before discussing the legislative history of the Administrative Procedure Act we wish to point out that this Court is in accord with the United States Supreme Court. *Penfield Co. of Calif. v. Securities and Exchange Commission,* 9th Cir. 143 F.2d 746, cert. den. 323 U.S. 768 (1944) enforced the subpena which became the basis for the contempt involved in the other *Penfield* case cited above. In doing so this court quoted from the *Endicott-Johnson* case by pointing out at page 751 that the evidence sought was not plainly incompetent or irrelevant to any lawful purpose. In other words, this court considered the question of jurisdiction before enforcing the subpena.

Legislative History.

The extensive legislative history of the Administrative Procedure Act is set forth in detail in the 423 pages of Senate Document No. 248, 79th Congress, 2nd Session.

Representative Walter in making the Committee Report to the House pointed out that this legislation was under consideration for more than 10 years. He went on to say, "certainly no measure of like character has had the painstaking and detailed study and drafting. Both the legislative and executive branches have participated and private interests of every kind have had an opportunity to present their views". Senate Document No. 248, p. 241.

The legislative history of the phrase "in accordance with law" reflects some of the views of these private interests. It meets them by saying that "in accordance with law" means "that no administrative subpena may be enforced beyond the lawful jurisdiction of the agency". The statement was made in connection with the Senate Committee Print of June, 1945. The full text is:

> "Private parties urge that after the word 'be' in the second sentence there be added, 'within the jurisdiction of the agency and otherwise', so that no administrative subpena may be enforced beyond the lawful jurisdiction of the agency. It is felt that 'in accordance with law' as now stated [in the revised text set forth above] means that. If adopted, the suggestion should be understood as not authorizing a complete pretrial in the courts of factual issues committed to exclusively administrative determination; courts should, instead, do no more than satisfy themselves that, legally upon the general factual situation shown, the agency has jurisdiction of the spe-

cific subject matter involved." Senate Document 248, page 28.

This interpretation as requiring the courts to satisfy themselves that the agency has jurisdiction continues throughout the legislative history. The Senate Committee Report on November 19, 1945 stated:

> "The subsection constitutes a statutory limitation upon the issuance or enforcement of subpenas in excess of agency authority or jurisdiction. This does not mean, however, that courts should enter into a detailed examination of facts and issues which are committed to agency authority in the first instance, but should, instead, inquire generally into the legal and factual situation and be satisfied that the agency could possibly find that it has jurisdiction. The subsection expressly recognizes the right of parties subject to administrative subpenas to contest their validity in the courts prior to subjection to any form of penalty for noncompliance." Senate Document 248, page 206.

The House Committee Report on May 3, 1946 said the same thing adding one sentence:

> "The section constitutes a statutory limitation upon the issuance or enforcement of subpenas in excess of agency authority or jurisdiction, in connection with any agency function or authority. It does not mean that upon contest courts should enter into a detailed examination of facts and issues which are committed to agency authority in the first instance; they should instead inquire generally into the legal and factual situation and be satisfied that the agency could lawfully have jurisdiction. The section expressly recognizes the right of parties subject to administrative

subpenas to contest their validity in the courts prior to subjection to any form of penalty for noncompliance. In such contests, the court is required to determine all relevant questions of law." Senate Document No. 248, page 265.

On May 24, 1956, when Representative Walter, a member of the House Judiciary Committee, gave an explanation of the entire Act he said:

"Subsection (c) of section 6 provides that, where Congress has authorized agencies to issue subpenas, private parties may secure them upon an equality with Government representatives and without any more than a general showing of relevance and reasonable scope of the information sought. Where administrative subpenas are contested, the court is to inquire into the situation and issue an order of enforcement only so far as the subpena is found to be in accordance with law. This is a definite statutory right and is applicable to subpenas of every kind addressed to any person under authority of any law. The effect of the subsection is thus to do more than merely restate the existing constitutional safeguards which in some cases, such as those involving public contractors—see *Endicott Johnson Corp. v. Perkins* (317 U.S. 501, 507, 509, 510 (1943)), have been held inapplicable. Also, the term 'in accordance with law' does not mean that a subpena is valid merely because issued with due formality. It means that the legal situation, including the necessary facts, demonstrates that the persons and subject matter to which the subpena is directed are within the jurisdiction of the agency which has issued the subpena." Senate Document No. 248, p. 363.

The order should be reversed because the District Court refused to consider the defense of no jurisdiction.

At least one thing is self-evident from the Supreme Court decisions and from the legislative history of Section 6(c). This one thing is the judicial duty of the District Court to consider the authority or jurisdiction of the agency over the subject matter of the administrative proceeding in an action to enforce an administrative subpena. Even those cases like *Endicott-Johnson Corp. v. Perkins,* supra, recognize that the evidence sought by the subpena must be competent and relevant to a lawful purpose of the agency which issued the subpena. In fact, the Government conceded in that case (as we pointed out before) that if the evidence sought "is not germane to any lawful purpose of inquiry" this alone would be an appropriate defense to an action to enforce the subpena.

Certainly the claim that the Federal Trade Commission has no jurisdiction as a matter of law over advertising of accident and health insurance by Fireman's Fund is a claim that the evidence sought by the subpena "is not germane to any lawful purpose of inquiry". This claim of no jurisdiction as a matter of law is purely a question of statutory interpretation; first, interpretation of Public Law 15 which divests the Federal Trade Commission of authority to regulate the business of insurance to the extent that such business is regulated by state law and second, interpretation of state law. These laws are matters of judicial notice. Therefore, as we said before, the claim of no jurisdiction is purely a matter of law; it does not depend upon any evidence sought by the subpena.

The Federal Trade Commission should concede (as the Government did in the *Endicott-Johnson* case) that this claim is an appropriate defense to the action to enforce the subpena. In any event, the Federal Trade Commission must admit that the District Court refused to consider this defense. Such refusal, in our opinion, is clearly contrary to law.

The subpena should not be enforced until this defense of no jurisdiction has been considered and determined. Therefore, the order should be reversed.

Advertising of accident and health insurance by Fireman's Fund is regulated by state law throughout the country. Therefore the Federal Trade Commission has no jurisdiction over such advertising.

The Federal Trade Commission rests jurisdiction in this proceeding on Public Law 15, 79th Congress (59 Stat. 33, 15 U.S.C. 1011-1015) sometimes known as the McCarran Act. The pertinent provisions of the Act are:

Section 1.

"Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several states."

Section 2.

"(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

"(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by

any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided,* That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law."

Section 3.

"(a) Until June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the Act of June 19, 1936, known as the Robinson-Patman Anti-discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

"(b) Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate or act of boycott, coercion, or intimidation."

The Act did two things. First, it provided a three-year moratorium until June 30, 1948 (originally January 1, 1948 but later extended by 61 Stat. 448) during which time the Federal Trade Commission had no jurisdiction over the business of insurance except in so far as the Sherman Act applied to boycotts, coercion or intimidation. Second, it provided, that after the moratorium Federal Trade Commission jurisdiction "shall be applicable to the

business of insurance to the extent such business is not regulated by state law."

The background of this legislation indicates an obvious congressional purpose to permit state regulation and to prohibit federal regulation if a state does regulate. The regulation of the insurance business had belonged historically to the states exclusively. This followed from the Supreme Court decision in the famous old case of *Paul v. Virginia,* 8 Wall. 168 (1868), which held that the business of insurance was not commerce. In 1944 the Supreme Court in *United States v. South-Eastern Underwriters Association,* 322 U.S. 533, contrary to *Paul v. Virginia,* held that the business of insurance was commerce and therefore that it might be subject to federal regulation. Congress reacted almost immediately by passing Public Law 15 creating a three-year moratorium and providing that thereafter the Federal Trade Commission could regulate the business of insurance but only to the extent that such business was not regulated by state law.

Fireman's Fund has contended from the beginning and still contends that advertising is fully regulated by state law and, therefore, that the Federal Trade Commission is without jurisdiction in its proceeding against the company. This contention rests on the law of California as the domiciliary state which imposes the basic limitations on the company's authority to do any insurance business anywhere and thereby regulates its activities everywhere. It also rests on the laws of the other 47 states and the District of Columbia. These local laws can and do impose additional regulation but none can lift the basic limitations imposed by California.

This contention of full regulation by state law might seem to impose a monumental task of analyzing the laws of all forty-eight states and of the District of Columbia. However, this task has been done for us in a companion proceeding. The Federal Trade Commission issued complaints against 40 or 41 companies. None of these cases had been decided (even initially by the Hearing Examiners) at the time of the hearing in the District Court. Since then there have been some initial decisions by Hearing Examiners although, as yet, no final order by the Commission in any contested case. These initial decisions agree that advertising is regulated by state law in all states except Mississippi, Rhode Island, Montana, Missouri and the District of Columbia.

We believe it is also regulated by state law in these five jurisdictions. We said in the court below (Tr. 86) that there were some states without regulation but further study of the state statutes indicates local regulation everywhere.

In this connection we repeat the statement by Senator McCarran when he pointed out that the question of jurisdiction "is one strictly of legal construction". He went on to say:

> "The inquiry will be, Is this practice regulated by state law? Not, is it effectively regulated, or is it wisely regulated; but simply is it regulated?" 94 Congressional Record No. 11, p. A 3214.

One of the Hearing Examiners, Mr. Frank Hier, in deciding against Federal Trade Commission jurisdiction except in these four states and the District of Columbia,

said in the *National Casualty Company* case (Federal Trade Commission Docket No. 6311):

> "* * * The factual basis in this proceeding behind the phrase 'to the extent not regulated by state law' is that 36 states have enacted the so-called 'Model Code' or 'Unfair Trade Practice Model Bill.' This 'Model Code' was enacted to implement the above-quoted McCarran Act, and prohibit as illegal, the dissemination of false, deceptive or misleading statements regarding insurance in terms as broad as Section 5 of the Federal Trade Commission Act, and at the same time in far more specific terms as well. The prohibition is implemented by appropriate enforcement and penalizing provisions, so that any licensed local agent may be haled before the state insurance commissioner to show cause why his employer's license to sell insurance in that state should not be revoked because of misrepresentation. In the opinion of the Hearing Examiner, they are fully effective to stop, within the state, the acts and practices charged here. Being an exercise of police power, these statutes obviously have no extraterritorial effect. In addition to these 36 states, eight others have statutes which, while couched in different language or varying somewhat in detail, are essentially the same in effect, as the 'Model Bill.' * * *"

There is no concurrent jurisdiction.

While we think the Federal Trade Commission will concede that 44 states (including California) have adequate state statutes, we expect the Commission to claim concurrent jurisdiction. In other words, we expect the Commission to claim jurisdiction over advertising used in California by a Michigan company and over advertising

used in Michigan by a California company, regardless of the extent of regulation by state laws in either state.

This theory of concurrent jurisdiction is contrary to Public Law 15, as Mr. Hier pointed out in the *National Casualty* case. We realize that an initial decision by a hearing examiner is not binding, but the logic of his reasoning is compelling. He said:

> "Counsel supporting the complaint contend for concurrent jurisdiction nation-wide, notwithstanding the McCarran Act. The contention is that Congress did not intend thereby to delegate its jurisdiction over interstate commerce to the states, that at most it gave the states concurrent jurisdiction within their borders over the same acts and practices, that the states cannot 'effectively' regulate such acts. The logical end-result of this contention, of course, is that if every state had enacted the 'Model Code,' so that there was not a square yard of unregulated territory under such state law and, therefore, no 'extent that such business is not regulated by state law,' that nevertheless, there is Federal jurisdiction. Another effect of this contention would necessarily be, that if the insurance commissioner of Pennsylvania, after summons and hearing, acting under Pennsylvania's Model Code, decides that respondent's representations are not false or misleading, nevertheless, the Federal Trade Commission, the next day, could decide that it was. This flies in the very teeth of the McCarran Act's prohibition that 'no act of Congress shall be construed to *invalidate, impair or supersede* any law enacted by any state, etc.' How it can be contended that such action under the Federal Trade Commission Act does not invalidate, impair or supersede the action under the state law is not made clear."

It might be added that the three-year moratorium provision in Public Law 15 is totally inconsistent with the idea that Congress meant to establish a system of concurrent jurisdiction. If Congress did not want the Federal Trade Commission to regulate the business of insurance before the various states had an opportunity to pass their own statutes, it cannot be said that Congress wanted the Federal Trade Commission to step in and regulate after the states had adopted their own schemes of regulation. The logic of this reasoning is supported by the Congressional debate incident to the enactment of Public Law 15. Senator McCarran said:

> "The moratorium would not be continued; but if in the meantime the States themselves had regulated the business of insurance, the Sherman and Clayton Acts and the other acts [obviously referring to the Federal Trade Commission Act] would not become effective." Conference Report on S. Bill 340—Vol. 91, Part 2, Cong. Rec. p. 1443.

Another Hearing Examiner, Mr. J. Earl Cox, in the *American Hospital* case, (Federal Trade Commission Docket No. 6237), also pointed out that Federal Trade Commission jurisdiction under Public Law 15, "is precluded to the extent that the states in which respondent is licensed to conduct its insurance business have regulatory statutes applicable to the acts and practices charged in the complaint to be false and deceptive." Mr. Cox supported his initial decision by quoting from various judicial decisions which have considered Public Law 15. The first and most important one is *Prudential Insurance Co. v. Benjamin,* 328 U.S. 408 (1946) which determined the con-

stitutionality of the law. In this decision the court, speaking through Mr. Justice Rutledge, said (pages 429-30) that by enacting Public Law 15,

> "Obviously, Congress' purpose was broadly to give support to the existing and future state systems for regulating and taxing the business of insurance. This was done in two ways. One was by removing obstructions which might be thought to flow from its own power, whether dormant or exercised, except as otherwise expressly provided in the Act itself or in future legislation. The other was by declaring expressly and affirmatively that continued state regulation and taxation of this business is in the public interest and that the business and all who engage in it 'shall be subject to' the laws of the several states in these respects."

In a later case, *Maryland Casualty Company v. Cushing,* 347 U.S. 409, 413 (1954) the Supreme Court, again speaking of Public Law 15, used these words:

> "Suffice it to say that even the most cursory reading of the legislative history of this enactment makes it clear that its exclusive purpose was to counteract any adverse effect that this court's decision in *U. S. v. South-Eastern Underwriters Association*, 322 U.S. 533, 88 L. ed. 1440, 64 S Ct 1162, might be found to have on State regulation of insurance."

Even later in *Wilburn Boat Co. v. Fireman's Fund Insurance Co.,* 348 U.S. 310, 319 (1955) the Supreme Court said:

> "* * * In the South-Eastern case, however, all the opinions had emphasized the historical fact that States had always been free to regulate insurance. The measure Congress passed shortly thereafter,

known as the McCarran Act, was designed to assure that existing state power to regulate insurance would continue. Accordingly, the Act contains a broad declaration of congressional policy that the continued regulation of insurance by the States is in the public interest, and that silence on the part of Congress should not be construed to impose any barrier to continued regulation of insurance by the States."

If the "exclusive purpose" of Public Law 15 was, as stated in *Maryland Casualty Company v. Cushing,* supra, to counteract any adverse effect of the decision of the *South-Eastern Underwriters* case on state regulation of insurance, there cannot be concurrent jurisdiction where there is regulation by state law. The *South-Eastern Underwriters* case held that the Sherman Act applied to an agreement by insurance companies fixing premium rates. It was argued that unrestricted competition in insurance results in financial chaos and public injury. The Supreme Court said, "Whether competition is a good thing for the insurance business is not for us to decide" and pointed out that exceptions to the Sherman Act "must come from the Congress." 322 US 561.

The adverse effect of this decision on state regulation of insurance was to make rate-fixing agreements subject to federal law. The obvious way to counteract this adverse effect was to make exceptions and thereby exclude such agreements from the Sherman Act.

Congress made exceptions, not only from the Sherman Act (except as to boycotts, coercion or intimidation) but also from the Federal Trade Commission Act and from the Clayton Act. Congress said, in Public Law 15, that

these federal statutes should be applicable to the business of insurance "to the extent that such business is not regulated by state law." If this means "concurrent jurisdiction", the adverse effect of the *South-Eastern Underwriters* case has not been counteracted; therefore, it must mean exclusive state jurisdiction to the extent of regulation by state law.

We have mentioned the extent of regulation in the 44 states. We shall now consider the laws in the other four states and the District of Columbia.

The Four States and the District of Columbia.

The business of insurance is the subject of comprehensive regulation in every state. Local statutes may vary but the states have exerted their powers to limits and in ways not sought generally to be applied in any other business. *Prudential Insurance Co. v. Benjamin,* supra. The dissenting opinion in the *South-Eastern Underwriters* case pointed out (322 US 590) that state regulation is "a going concern."

This applies not only to the 44 states mentioned above but also to the other four states and to the District of Columbia. We could argue that comprehensive regulation of the insurance business by every state precludes Federal Trade Commission jurisdiction over every phase of the insurance business.

However, it is not necessary to discuss the over-all effect of these comprehensive schemes of state regulation. The specific prohibitions against misrepresentation and against false or deceptive statements in the statutes of the four states and of the District of Columbia provide

ample support for stating that advertising of accident and health insurance is regulated by these state laws. The fact that a statute is part of a criminal code instead of an insurance code or applies to all advertising does not make it any less applicable to advertising of accident and health insurance.

Missouri.

Mr. Hier, in the *National Casualty* case, included Missouri as one of the four states without regulation. However, Mr. Cox, in the *American Hospital* case, pointed out that the company (a Texas corporation) was licensed to do business in Missouri and, therefore, bound by the statutes of Missouri. He said:

> "These statutes appear to be adequate to protect the residents of that state from false, misleading or deceptive insurance advertising practices, and therefore are regulatory of the extent prescribed by Public Law 15 as being proscriptive of the applicability of the Federal Trade Commission Act."

He was referring to Chapter 561, entitled "Crimes and Punishment," of the laws of Missouri and particularly to Section 561.660, entitled "Publication of Untrue, Misleading or Deceptive Advertising—Penalty." This is a general criminal statute making it unlawful to publish, disseminate or circulate any advertisement which contains any assertion, representation or statement of fact which is untrue, deceptive or misleading. The violation of the statute is a misdemeanor punishable by fine or imprisonment, or both. The statute is set forth in the appendix to this brief.

The American Hospital and Life Insurance Company, as its name implies, was authorized to do life insurance business as well as health and accident insurance business. Therefore, Mr. Cox also referred to the Missouri statutes which regulate life insurance business specifically but do not mention accident and health insurance. Fireman's Fund does not write life insurance as such, but we should point out that accident and health insurance with death benefits is a form of life insurance. In any event, a general statute providing criminal penalties for false advertising includes advertising of accident and health insurance and therefore regulates such advertising to the extent prescribed by Public Law 15 as being proscriptive of the applicability of the Federal Trade Commission Act.

Rhode Island.

The *American Hospital* case did not involve any activities in the state of Rhode Island; therefore, Mr. Cox had no occasion to consider Rhode Island law. However, Rhode Island, like Missouri, has a general statute (Chapter 612, Section 54) providing criminal penalties for any false advertising. The statute is set forth in the appendix to this brief.

Therefore, Rhode Island, like Missouri, has regulated the advertising of accident and health insurance to the extent prescribed by Public Law 15 as being proscriptive of the applicability of the Federal Trade Commission Act.

District of Columbia.

Again Mr. Cox had no occasion to consider the laws of the District of Columbia in the *American Hospital* case. These laws, like the laws of Missouri and Rhode

Island, include a general statute (Section 22-1411, District of Columbia Code) prohibiting any false advertising and providing criminal penalties. The statute is set forth in the appendix to this brief.

Therefore, the District of Columbia, like Missouri and Rhode Island, has regulated the advertising of accident and health insurance to the extent prescribed by Public Law 15 as being proscriptive of the applicability of the Federal Trade Commission Act.

Montana.

Montana, as far as we know, has no statute specifically regulating advertising of accident and health insurance, although it does have a statute (Section 40-1939, Montana Revised Code) providing that no life insurance company shall issue any circular or statement misrepresenting the terms, benefits or advantages of any policy issued by such corporation. Montana also has a statute (Section 94-1819, Montana Revised Code) prohibiting advertising regarding "the quality or price of goods, wares or merchandise" offered for sale to the public. "Merchandise" is defined by Webster to include objects of commerce, and insurance, at least since the *South-Eastern Underwriters* case, is an object of commerce.

Further, Section 40-1106 of the Revised Code of Montana, provides that if the insurance commissioner finds on examination, hearing or other evidence that any insurance company doing business in Montana uses methods that are such "as to render its operations hazardous to the public or its policy holders" the insurance commissioner shall suspend or revoke all certificates of authority

granted to the company and to its officers and agents. We think that a false statement regarding the benefits of accident and health insurance policies is "hazardous to the public", who might be induced to purchase accident and health insurance, relying upon the false statement. It might also be hazardous to the present holders of policies if it was sufficiently widespread to subject the company to litigation which might adversely affect its financial ability to pay claims.

These statutes are set forth in the appendix to this brief.

Under all of these circumstances, it seems to us that Montana has regulated the business of accident and health insurance to the extent prescribed by Public Law 15 as being proscriptive of the applicability of the Federal Trade Commission Act.

Mississippi.

Mississippi is now in the process of becoming a "model act" state. The proposed statute is House Bill 145 introduced in the Mississippi House of Representatives on January 25, 1956, and now pending before the Insurance Committee. We anticipate favorable action and hope to report to this court in our reply brief or at oral argument that Mississippi is completely regulated by state law. However, Mississippi does have statutes which prohibit misrepresentations. Section 5683 of the Mississippi Code dealing with insurance provides:

> "Any solicitor, agent, examining physician or other person who shall knowingly or willfully make any false or fraudulent statement or representation in or

with reference to any publication for insurance, or who shall make any such statement for the purpose of obtaining fee, commission, money or benefit in any corporation, transacting business under this chapter, shall be guilty of a misdemeanor, and upon conviction shall be punished by a fine of not less than one hundred dollars, nor more than five hundred dollars, or imprisonment in the county jail for not less than thirty days." (1906)

Section 2149 of the Mississippi Code dealing with Crimes and Misdemeanors, provides:

"Every person whom with intent to cheat or defraud another, shall designedly, by color of any false intoken or writing, or by another false pretense, obtain the signature of any person to any written instrument, or obtain from any person any money, personal property, or valuable thing, upon conviction thereof, shall be punished by imprisonment in the penitentiary not exceeding three years, or in the county jail not exceeding one year, and by fine not exceeding three times the value of the money, property, or thing obtained."

It has been suggested that these statutes do not apply to a corporation and therefore are inapplicable to the present situation. However, they do apply to any false or fraudulent statement or representation by an "agent". Therefore, in our opinion, they regulate Fireman's Fund which disseminates advertising in Mississippi only through independent local agents or brokers, each of whom is separately licensed under Mississippi law.

In our opinion there is not a square yard of territory in the United States unregulated by local state law, with

the possible exception of Mississippi. Obviously the only lawful inquiry by the Federal Trade Commission must concern acts and practices not regulated by state laws; evidence of acts and practices in states which do regulate would not be germane to such an inquiry. If there is any unregulated territory the subpena should be limited to acts and practices there and should be quashed in so far as it seeks evidence of activities in other states or in the District of Columbia.

Direct Mail Advertising.

Mr. Hier, in the *National Casualty* case, points out that the company did something less than 5% of its business direct by mail and that state law cannot control the United States mails. He concludes therefrom that the Federal Trade Commission has jurisdiction over the direct-by-mail portion of the company's business, citing *United States v. Sylvanus,* 7th Cir., 192 F. 2d 96 (1951).

We think this is wrong. Certainly a state can regulate advertising by anyone doing business within its borders, whether such advertising is disseminated by mail or by local agents. *Robertson v. People of the State of California,* 328 U.S. 440 (1946) affirmed the conviction of a California resident for violating the California statutes requiring an agent or broker to have a license under the California insurance code. Robertson was acting for an Arizona company not admitted to do business in California. The court pointed out that literature regarding the company's insurance business apparently was mailed from the home office. In upholding the conviction, the court said, at pages 458-459:

> "* * * the commerce clause is not a guaranty of right to import into a state whatever one may please, absent a prohibition by Congress, regardless of the effects of the importation upon the local community. This is true whether what is brought in consists of diseased cattle or fraudulent or unsound insurance."

See also *Travelers Health Association v. Commonwealth of Virginia*, 339 U.S. 643 (1950), which upheld a Virginia cease and desist order against a Nebraska association whose only office was in Omaha, Nebraska, from which it conducted a mail-order health insurance business into other states, including Virginia.

In any event the fact that a state cannot directly regulate the mails as such does not necessarily mean that the Federal Trade Commission has been given power to do so. *United States v. Sylvanus* is not a Federal Trade Commission case. It did not involve any violation of the Federal Trade Commission Act or of any other act administered by the Commission. It was a mail fraud case.

The defendants contended that the indictment was defective because of Public Law 15, claiming that their activities were regulated by the laws of Illinois, the state in which they did business. The court overruled this contention, stating (192 F2d 100):

> "However, we believe that it can not properly be said that this indictment has to do with the regulation of insurance business in Illinois. Rather it has to do with the question of whether defendants have used the mails in pursuance of a scheme so to manipulate their authorized regulated business in Illinois as to result in fraudulent deception of its prospective

policy holders. * * * It is immaterial that the fraudulent plan itself is outside the jurisdiction of Congress (citing authority), or that the scheme charged involved a transaction forbidden by the laws of the state."

Fireman's Fund has alleged in its answer in the administrative proceeding (Tr. 61) that it does not sell or offer to sell any accident and health insurance by mail or by any other direct means, but at all times sells such insurance only through various independent agents and independent brokers, each of whom is licensed to do business and separately regulated by the state in which the independent agent or independent broker is located. We think the Federal Trade Commission will admit that this is true, although the administrative complaint alleges in paragraph 4 (Tr. 10) that the statements were disseminated "through the United States mails and by other means or through its agents in commerce between and among the various states of the United States."

It should be remembered that authority to regulate the use of the mails has been delegated to the Postmaster General who may issue fraud orders to prevent any person or company from using the mails to obtain money or property by means of false representation or promises. 26 Stat. 466 as amended by 28 Stat. 964, 39 U.S.C. 259.

While we think that the Federal Trade Commission has no authority to regulate the use of the mails as such, if the court disagrees with us the subpena should be limited to evidence of the use of the mails in direct mail advertising and should be quashed as to evidence of other acts or practices.

Fireman's Fund is a California corporation. Its advertising of accident and health insurance is regulated by California law everywhere. Therefore, the Federal Trade Commission has no jurisdiction over such advertising anywhere.

Congress in passing Public Law 15 authorized the states to regulate the business of insurance and prohibited the Federal Trade Commission from doing so to the extent that such business is regulated by state law. The power to regulate thus granted to each state is the power to regulate commerce, and as the Supreme Court said in *United States v. Darby,* 312 U.S. 100, 113 (1941),

> "The power to regulate commerce is the power 'to prescribe the rule by which commerce is governed'. Gibbons v. Ogden, 9 Wheat. (US) 1, 196, 6 L.ed. 23, 70. It extends not only to those regulations which aid, foster and protect the commerce, but embraces those which prohibit it."

This power to aid, foster and protect the business of insurance should be exercised with appropriate regard to the public, to the companies, and to the policy holders. It should be used to promote the growth of the business of insurance and to insure the safety of such business.

California as the domiciliary state of Fireman's Fund should regulate Fireman's Fund not only with appropriate regard to the citizens of California but also with appropriate regard to the growth and safety of the company. California, as we pointed out before, created Fireman's Fund by granting it authority to be a corporation and to do insurance business. This grant of authority governs Fireman's Fund in each of the 48 states and the District of Columbia. It carries with it all limitations and prohibitions imposed by California.

One of the limitations California has imposed on Fireman's Fund prohibits the company from causing or permitting any advertising containing any misrepresentations regarding the terms of a policy issued by the company or regarding the benefits or privileges promised under such a policy. This prohibition follows Fireman's Fund everywhere and therefore excludes authority of the Federal Trade Commission over such advertising anywhere.

This thought seems to startle some people. Why should it? A corporation is an artificial being created by state law. A natural person has certain inherent rights and powers; a corporation does not. A corporation may do those things (but only those things) authorized by laws of the state which creates it.

Everyone should admit that a California insurance corporation cannot do a banking business in California or anywhere else. Further, a California corporation authorized to issue 100,000 shares of common stock and no other, cannot issue more common stock or issue shares of any other class in California or in any other state. Why, then, should anyone be startled by the fact that a California insurance company is governed and limited everywhere by California law?

There is nothing in Public Law 15 which suggests that the regulation of the business of insurance must be by local state law. It should therefore be self-evident that California by prohibiting false advertising by Fireman's Fund everywhere has excluded Federal Trade Commission authority over such advertising anywhere.

The pertinent statute is Section 780 of the California Insurance Code, which reads:

> "An insurer or officer or agent thereof, or an insurance broker or solicitor, shall not cause or permit to be issued, circulated or used, any misrepresentation of the following:
>
> "(a) The terms of a policy issued by the insurer or sought to be negotiated by the person making or permitting the misrepresentation.
>
> "(b) The benefits or privileges promised thereunder.
>
> "(c) The future dividends payable thereunder."

Extremely strong enforcement sections are provided to insure compliance with Section 780. Violation of Section 780 by any person is made a misdemeanor punishable by fine or imprisonment (Section 782). More important, a violation of Section 780 by the company may result in suspension of the insurer's certificate of authority to do the class of insurance in respect to which the violation occurred (Section 783.5) and without a certificate of authority a company may not transact any insurance business (Section 700). To do so would be a misdemeanor (Section 10500). In addition, the Insurance Commissioner, who is commanded by statute (Section 12926) to require from every insurer a full compliance with the provisions of the Code, may bring an action to enjoin violations of any law including Section 780 (Section 12928.6). These statutes (other than Section 780 quoted above) are set forth in the appendix to this brief. These sections of California law include California in the category of states (other than "Model Act" States) having

statutes regulatory of the business of insurance to the extent prescribed by Public Law 15 as being proscriptive of the applicability of the Federal Trade Commission Act.

Although there is no case authority directly in point on either side, it seems clear that Insurance Code Section 780 and the related sections are sufficiently broad to cover dissemination of misleading advertising outside of California by a California insurer. The section does not purport to limit itself only to advertising distributed within the confines of California. The Insurance Code taken as a whole gives ample indication that Section 780 was not intended to refer only to advertising disseminated within the borders of California, for where particular sections are intended to operate only when the consumer or insured interest are within the state they make this clear by a specific statement. Thus, for instance, rebates of premiums are forbidden by Section 750, but it is expressly provided that this applies only where the subject matter of the insurance is located in California. If the Legislature had desired to limit Section 780 only to situations where California residents receive the false advertising, a similar express limitation would have been written in the statute.

Very important is the fact that Section 780 prohibits not only the actual dissemination of misrepresentations, but also *causing* or *permitting* them to be issued. Since Fireman's Fund has its main office in California, any representations that it makes are caused or permitted in California regardless of where they are disseminated. It would be disregarding the plain wording of the statute to construe it to apply only to misrepresentations *issued* locally.

Although no California decision has yet considered the precise question of whether Section 780 prohibits a California insurer from using false advertising in other states, we expect the California Attorney General to file a brief amicus on behalf of the California Insurance Commissioner, construing Section 780 in support of our contention that this section applies to Fireman's Fund everywhere. In fact, the California Attorney General is now making this contention in the case of *Foster v. McConnell*, No. 422572 in the Superior Court of the State of California in and for the City and County of San Francisco. This is an action by Mr. Foster for a writ of mandate to compel the Insurance Commissioner to restore Mr. Foster's license which had been revoked because of misrepresentations made outside of California. The misrepresentations were made at Fort Ord, a military reservation, which is as much outside of California as is any other state or the District of Columbia.

The interpretation by the Attorney General, especially in the absence of any direct judicial authority, is most persuasive. As stated in 6 Cal. Jur. 2d 97:

> "The opinions of the attorney general are not of controlling authority, but in the light of the relation of the office to the general government, they are regarded as having quasi-judicial character and are accorded substantial weight by the courts." (Citing *People v. Shearer,* 30 C. 645; *Carter v. Commission on Qualifications,* 14 C. 2d 179, 93 P. 2d 140).

Despite the lack of direct judicial authority, there is no absence of analogy. In *People v. Lindsay,* 86 Colo. 458, 283 P. 539 (1929), for example, it was held that a

statute which provided that the Judge of the Juvenile Court should not "act as an attorney or counselor at law," without specifying that the prohibition was limited to Colorado, applied to the practice of law in the courts of New York. Similarly, in *In Re Porep,* 60 Nev. 393, 111 P.2d 533 (1941), the court held that a Rule of Professional Conduct of the State Bar of Nevada reading "A member of the state bar shall not solicit professional employment by advertising or otherwise" prohibited a Nevada attorney from advertising his services in California.

The so-called "extraterritorial" effect of the California statutes is not unconstitutional.

The so-called extraterritorial effect of the California regulation of its domestic insurance corporations is not unconstitutional. Modern cases have shown an increasing liberality in allowing states to regulate where under the old formulæ represented by cases like *Allgeyer v. Louisiana,* 165 U.S. 578 (1897) and *St. Louis Cotton Compress Co. v. Arkansas,* 260 U.S. 346 (1922), the regulations might have been considered to constitute a violation of the due process clause of the Fourteenth Amendment because of their extraterritorial effects. It is well settled now that a state may apply its own law to acts which occur outside of its borders where interests of the state are in some manner affected by these actions.

Thus, in *Hoopeston Canning Co. v. Cullen,* 318 U.S. 313 (1943), the court upheld the validity of certain provisions of the New York Insurance Law regulating foreign reciprocal insurance associations where property in New York was insured, despite the fact that the actual business regulated was transacted in Illinois. Said the court at p. 320:

"These regulations cannot be attacked merely because they affect business activities which are carried on outside the state."

In *Alaska Packers Asso. v. Industrial Accident Com.*, 294 U.S. 532 (1935), the Supreme Court held that the California Workmen's Compensation statute might be applied where the contract of employment was entered into in California although the particular employee involved was a nonresident alien and the accident occurred in Alaska. Here it would seem that California contacts were of considerably less weight than those of Alaska. Nevertheless, the California courts were not precluded from applying California law, despite its extraterritorial effect.

Recently in *Watson v. Employer's Liability Assur Corp.*, 348 U.S. 66 (1954), the Supreme Court upheld a Louisiana direct action statute as applied to an insurance contract entered into in another state between two foreign corporations. The court rejected the argument that it violated the due process clause because of its extraterritorial application, holding that where a state has a substantial interest in applying its own law it may do so constitutionally.

Other cases applying similar standards to uphold state regulation attacked on the ground of extraterritoriality include *Osborn v. Ozlin,* 310 U.S. 53 (1940) and *Traveler Health Association v. Virginia,* 339 U.S. 643 (1950).

It is clear that the so-called "extraterritorial" effect of the California regulatory statutes is constitutional. Hence, California regulation alone prevents the Federal

Trade Commission from assuming jurisdiction over Fireman's Fund anywhere, and so the subpena should be quashed even if there is any place outside of California unregulated by local law.

CONCLUSION.

As we conclude, it is well to bear in mind that Congress by passing Public Law 15 placed definite limitations on the jurisdiction of the Federal Trade Commission over the business of insurance. Congress did this by saying that the Federal Trade Commission could regulate the business of insurance "to the extent that such business is not regulated by state law". There is no suggestion of dual or concurrent regulation. Instead, the obvious purpose of Public Law 15 was to permit the states to take back (except as to boycotts, etc.) the exclusive jurisdiction which the states had prior to the *South-Eastern Underwriters* case.

This exclusive jurisdiction includes regulation of advertising in the accident and health insurance field. If such advertising by Fireman's Fund is regulated by state law everywhere (by local law or by California law), the Federal Trade Commission has no jurisdiction, and the subpena should be quashed because the evidence sought by the subpena could not be germane to any lawful purpose or inquiry of the Commission. If the court finds that there is any place where such advertsiing is unregulated by state law, the evidence to be produced should be limited to such place, because evidence of acts or practices elsewhere would not be competent or relevant.

In any event, the order supporting the subpena should be reversed because the District Court refused to consider the defense of no jurisdiction and enforced the subpena looking only to the formalities without any regard as to whether the administrative proceeding was lawful or unlawful. The Government in *Endicott-Johnson Corp. v. Perkins,* supra, conceded that this defense of unlawful inquiry is an appropriate defense. Appellant James F. Crafts is entitled to have this defense judicially determined before being required to obey the subpena.

Dated: March 15, 1956.

Respectfully submitted,

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and

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(Appendix Follows.)

Appendix.

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Appendix

CALIFORNIA INSURANCE CODE.

Section 700. *Admittance required; issuance of certificate; compliance with requirements; hearing.* A person shall not transact any class of insurance business in this State without first being admitted for such class. Such admission is secured by procuring a certificate of authority from the commissioner. Such certificate shall not be granted until the applicant conforms to the requirements of this code and of the laws of this State prerequisite to its issue. After such issue the holder shall continue to comply with the requirements as to its business set forth in this code and in the laws of this State. Where a hearing is held under this section the proceedings shall be conducted in accordance with Chapter 5 of Part 1 of Division 3 of Title 2 of the Government Code, and the Commissioner shall have all the powers granted therein.

Section 750. *Rebate of premium.* An insurer, insurance agent, broker, or solicitor, personally or by any other party, shall not offer or pay, directly or indirectly, as an inducement to insurance on any subject matter in this State, any rebate of the whole or part of the premium payable on an insurance contract, or of the agent's or broker's commission thereon, and such rebate is an unlawful rebate.

Section 782. *Misdemeanor.* Any person violating the provisions of section 780 or 781 is guilty of a misdemeanor and punishable by a fine not exceeding one hun-

dred dollars ($100) or by imprisonment not exceeding six months.

Section 783.5. *Suspension of certificate of authority.* If an insurer knowingly violates any provision of sections 780 or 781, or knowingly permits any officer, agent, or employee so to do, the commissioner, after a hearing in accordance with the procedure provided in section 704, may suspend the insurer's certificate of authority to do the class of insurance in respect to which the violation occurred.

Section 10500. *Transaction of business without certificate; misdemeanor.* Every person not expressly exempted by the provisions of this code that transacts life or disability insurance without a valid and unrevoked certificate of authority or without a valid and unrevoked certificate of exemption issued pursuant to this article, is guilty of a misdemeanor. Every employee, officer or agent of any person who knowingly assists any person in the transaction of insurance in violation of the provisions of this code, is guilty of a misdemeanor.

Section 12926. *Requiring compliance with code.* The commissioner shall require from every insurer a full compliance with all the provisions of this code.

Section 12928.6. *Suit for injunction.* Whenever the commissioner believes, from evidence satisfactory to him, that any person is violating or about to violate any provision of this code or any order or requirement of the commissioner issued or promulgated pursuant to authority expressly granted the commissioner by any provision of this code or by law, the commissioner may bring an actio

n the name of the people of the State of California in he superior court of the State of California against such person to enjoin such person from continuing such violation or engaging therein or doing any act in furtherance hereof. In such action an order or judgment may be entered awarding such preliminary or final injunction as s proper.

DISTRICT OF COLUMBIA.

District of Columbia Code,
Section 22-1411.

Fraudulent Advertising.

It shall be unlawful in the District of Columbia for ny person, firm, association, corporation, or advertising gency, either directly or indirectly, to display or exhibit o the public in any manner whatever, whether by handill, placard, poster, picture, film, or otherwise; or to nsert or cause to be inserted in any newspaper, magazine, r other publication printed in the District of Columbia; r to issue, exhibit, or in any way distribute or disseminate to the public; or to deliver, exhibit, mail, or send o any person, firm, association, or corporation any false, ntrue, or misleading statement, representation, or advertisement with intent to sell, barter, or exchange any goods, wares, or merchandise or anything of value or to deceive, mislead, or induce any person, firm, association, or corporation to purchase, discount, or in any way invest in or accept as collateral security any bonds, bill, share of stock, note, warehouse receipt, or any security; or with the purpose to deceive, mislead, or induce any person,

firm, association, or corporation to purchase, make any loan upon or invest in any property of any kind; or use any of the aforesaid methods with the intent or purpose to deceive, mislead or induce any other person, firm, or corporation for a valuable consideration to employ the services of any person, firm, association, or corporation so advertising such services.

MISSOURI.

Vernon's Annotated Missouri Statutes,
Section 561.660.

Publication of untrue, misleading or deceptive advertisements—penalty.

1. Any person, firm, corporation, or association who with intent to sell or in anywise dispose of merchandise securities, service or anything offered by such person firm, corporation or association, directly or indirectly, to the public for sale or distribution or with intent to increase the consumption thereof or to induce the public in any manner to enter into any obligation relating thereto or to acquire title thereto or an interest therein, makes publishes, disseminates, circulates or places before the public, or causes, directly or indirectly, to be made, published, disseminated, circulated or placed before the public in this state, in a newspaper or other publication or in the form of a book, notice, handbill, poster, bill, circular, pamphlet, or letter or in any other way, an advertisement of any sort regarding merchandise, securities, service or anything so offered to public, which advertisement contains any assertion, representation or statement of fact

ıich is untrue, deceptive or misleading, shall be guilty a misdemeanor.

2. And shall upon conviction thereof be punished by fine of not less than twenty-five dollars nor more than e hundred dollars, or by imprisonment in the county l not less than ten days nor more than ninety days, or both such fine and imprisonment; providing, that thing herein shall apply to any proprietor or publisher any newspaper or magazine who publishes, dissem-ates or circulates any such advertisement without the owledge of the unlawful or untruthful nature of such vertisement.

MONTANA.

Montana Revised Code,
Section 94-1819.

False statements regarding merchandise.

It shall be unlawful for any person, corporation, copart-rship, or association of individuals to make any false tement regarding the quality or price of goods, wares merchandise in any advertisement, circular, letter, ster, handbill, display cards, or other written or printed tter by means of which such goods, wares or merchan-se are offered for sale to the public.

Montana Revised Code,
Section 40-1106.

Publication of examination—revocation of license.

When the commissioner of insurance deems it to the terest of the public, he may publish the result of any

examination or investigation in a newspaper of genera
circulation published at the state capital. If the com
missioner finds upon examination, hearing, or other evi
dence, that any insurance company, including surety com
panies, organized in this state, or in any other state, terri
tory, or foreign country, is in an unsound condition, o
has failed to comply with the law or with the provision
of its charter, or that its condition is, or its methods are
such as to render its operations hazardous to the publi
or to its policyholders, or that its actual assets, exclusiv
of its capital, are less than its liabilities, or if its officer
or agents refuse to submit to examination, or to perfor
any legal obligation relative thereto, or refuse on behal
of the company to pay the examination charges, he shal
suspend or revoke all certificates of authority grante
to said insurance company, and to its officers or agents
and shall cause notice thereof to be published in one o
more daily newspapers of general circulation publishe
at the state capital, and no new business shall thereafte
be done by it or its agents in this state while such defau
or disability continues, nor until its authority to do bus
ness is restored. Before suspending or revoking the ce
tificate of authority of any such company, the commi
sioner shall, unless it is insolvent or its capital impaire
grant it fifteen days in which to show cause why suc
action should not be taken. Any insurance company, i
cluding surety companies, organized under the laws
this state, or any other state, territory, or foreign countr
whose certificate of authority has been suspended or r
voked by the commissioner, may, within fifteen days ther
after, appeal from said order to the district court, whi
court, upon the filing of the proper petition, shall cau

e record and orders of the commissioner to be brought fore it, and upon a hearing of the case by the court novo, the court shall either confirm or revoke the order the commissioner, as the law and the fact of the case ay warrant.

RHODE ISLAND.

General Laws of Rhode Island,
Ch. 612, Sec. 54.

No person, firm, corporation or association, with intent to sell, or in anywise dispose of merchandise, securities, service or anything offered by such person, firm, rporation or association, directly or indirectly, to the ublic for sale or distribution, or with intent to increase e consumption thereof, or to induce the public in any anner to enter into any obligation therefor or to acquire tle thereto, or any interest therein, shall make, publish, sseminate, circulate, or place before the public, or cause, irectly or indirectly, to be made, published, disseminated, rculated or placed before the public, in this state, in newspaper or other publication, or in the form of a ook, notice, handbill, poster, bill, circular, pamphlet, letr, or in any other way, an advertisement of any sort egarding merchandise, securities, service, or anything so ffered to the public, which advertisement contains any ssertion, representation, or statement of fact, which is ntrue, deceptive or misleading, or which uses, with or ithout the use of the word "value" or the word "worth," r other synonymous term, any word or words, figure or igures, which falsely or fraudulently convey or would

reasonably so convey to a reader the meaning that the merchandise, securities, service, or other things so advertised are intrinsically worth more than, or were previously sold or offered for sale at a price higher than the price quoted in said advertisement. For the purpose of this section the worth or value of any merchandise securities, services or other things so advertised, shall be taken to be the prevailing market price, wholesale if offered at wholesale, retail if the offer was at retail at the time of publication of such advertisement in the locality wherein the advertisement was published. No person firm, corporation or association, with intent to profit, directly or indirectly thereby, shall place, or cause or produce an advertisement to be placed in or affixed to a newspaper, without the consent of the publisher of said newspaper; and in any way calculated to lead the reader thereof to believe that such advertisement was circulated by such publisher. The placing of an advertisement, notice, circular, pamphlet, card, handbill, printed notice of any kind in or the affixing thereof to a newspaper is presumptive evidence that the person or persons, or corporation or corporations, whose name or names appear therein as proprietor, advertiser, vendor, or exhibitor or whose goods, wares and merchandise are advertised therein, cause or procured the same to be so placed or affixed with intent to profit thereby. Any person, firm corporation or association who shall violate any of the provisions of this section shall be fined not less than $50.00 nor more than $300.00, or be imprisoned not more than 90 days or shall suffer both such fine and imprisonment. (P.L. 1928, Chap. 1199, amending P.L. 1914, Chap. 1073.)